

TESTIMONY OF

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Before the

Subcommittee on Housing and Transportation
Committee on Banking, Housing and Urban Affairs
United States Senate

Hearing on

"The Real Estate Appraisal Industry"

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Chairman Allard, Ranking Member Reed and Members of the Housing and Transportation Subcommittee:

Introduction

The American Society of Appraisers (ASA) greatly appreciates the opportunity to provide its views to the Subcommittee on “The Real Estate Appraisal Industry.” We also appreciate the Subcommittee’s interest in examining the impact of Title XI of FIRREA on the real estate appraisal profession, particularly with regard to protecting federal financial interests and assuring the safety and soundness of real estate-related financial transactions in our marketplace. My name is Eugene Kaczowski, and I serve as president of the American Society of Appraisers. I am an Accredited Senior Appraiser in the business valuation discipline and a vice president with American Appraisal Associates, a full-service valuation consulting firm.

ASA is our nation’s only multidiscipline professional appraisal society that teaches, tests and credentials its members in every major field of the appraisal profession, including residential and commercial real property valuation; business enterprise valuation; machinery and technical specialties; and valuations of fine arts, antiques, gems and jewelry. Attached to my testimony is a fact sheet providing additional information on ASA.

Summary of Views

The American Society of Appraisers believes that the state of the real estate appraisal profession is generally good and that enactment of Title XI of FIRREA in 1989 was, and

continues to be, an indispensable and positive force in professionalizing the nation's real estate appraisers. We are convinced that today's real estate appraisers, as a group, are far better educated, more competent and are held to a higher standard of ethics and accountability than their pre-FIRREA predecessors. Having said that, ASA also believes that there are some serious problems in the regulated environment in which today's real estate appraisers function and that Title XI needs to be modernized and tightened in order to correct those problems.

The Pre-FIRREA World of Real Estate Appraisers

Before discussing these problem areas and recommending some approaches to addressing them, I'd like to take just a moment to revisit the conditions that made up the real estate appraisal industry prior to the enactment of Title XI. Pre-FIRREA almost anyone could perform real estate valuations merely by declaring that they were competent to do so. At that time, there were few, if any, federal requirements specifying the education, training, experience and other skill sets necessary for an individual to estimate the market value of real estate collateralizing residential and commercial loans-sometimes totaling millions of dollars-made by federally insured financial institutions, guaranteed by federal agencies like the FHA and VA or sold to investors in the secondary financial markets by the GSEs or their private sector counterparts. Only a handful of states had appraiser licensing programs of any kind. For the few that did, qualification requirements were inconsequential and non-licensed individuals could continue to value real estate for virtually all transactions. These were the conditions that added billions of dollars in bailout costs to U.S. taxpayers when the savings and loan and banking industry

crises occurred in the mid-to-late 1980s. What Congressional oversight committees, the General Accounting Office (GAO) and investigative reporters found when they examined the causes and consequences of the collapse was that in a shockingly large percentage of cases, the collateral for billions of dollars in defaulted real estate loans had been grossly overvalued by appraisers, sometimes because of incompetence and sometimes because they were pressured by lenders or developers to manufacture values sufficiently high to make the deal go.

An important component of Congress' package of responses to the debacle and to the role of faulty and fraudulent real estate appraisals was the enactment of FIRREA and its Title XI system of state appraiser certification and licensing.

What's Working in the Current Title XI System

ASA believes that there is much good public policy incorporated into Title XI. We think that the certification and licensing system correctly balances the interests and the roles of state and federal governments and the private sector in professionalizing real estate appraisers and making them accountable for their actions. Under the current system, states are responsible for certifying and licensing appraisers and for disciplining them when they are found to be incompetent or dishonest. Title XI invests in the not-for-profit Appraisal Foundation, which is responsible for promulgating uniform appraisal standards (the Uniform Standards of Professional Appraisal Practice or USPAP) and for establishing uniform qualification requirements for the certification of appraisers. Finally, because the integrity and accuracy of real estate appraisals impact so many important federal programs and financial interests, Title XI leaves to the federal

government, through the Appraisal Subcommittee, responsibility for overseeing the effectiveness of the state appraiser regulatory programs and standards-setting work of the Appraisal Foundation.

With a few noteworthy exceptions, which I will address, ASA believes Title XI's real estate appraiser certification and licensing system is working well. Today, there are more than an adequate number of state-certified and licensed real estate appraisers providing the uniform valuation services that are essential to our nation's economy and to the cost-efficient operation of federal programs. Under the current system, these appraisals are being performed in what we believe is a timely and cost-effective manner, utilizing valuation methodologies that are uniform across every region of our country.

What Needs Correcting in the Title XI System

Although we believe that Title XI is accomplishing its intended public policy purposes, there are some serious problems with the current system that ASA finds troubling and that we wish to bring to the Subcommittee's attention—including the failure of a small number of important federal agencies to take advantage of it. Some of these problem areas fall within the clear jurisdiction of the Senate Banking Committee; others may require the attention of other committees of the Congress. These are our concerns.

(1) Problem: The current membership of the federal Appraisal Subcommittee is too narrowly drawn. The Subcommittee lacks representation from non-banking and non-housing federal agencies that administer programs or have regulatory responsibilities

that rely on the competency of real estate appraisers and the appraisals they perform. The Department of Interior (e.g., land exchanges and sales, conservation easements), the Department of Transportation (e.g., right-of-way issues), the Internal Revenue Service (e.g., charitable contributions of real estate and real estate assets in estate and gift tax returns) and the Securities and Exchange Commission (e.g., financial reports of public companies where real estate holdings are material) are examples of federal agencies whose activities regularly intersect the world of real estate appraisals.

Recommended solution: Although this issue needs to be analyzed in some depth, ASA believes that expanding the membership of the Appraisal Subcommittee would more accurately reflect the range of federal interests in the work of real estate appraisers—and greatly maximize the benefits that the federal government receives from professional real estate appraisals.

(2) Problem: The Appraisal Subcommittee lacks appropriate rulemaking powers necessary to ensure that states regulate appraisers in a way that is uniform and fully consistent with Title XI requirements. Time and experience have demonstrated that the authority of the Appraisal Subcommittee to ensure compliance with Title XI needs to be enhanced. Under existing law, the Subcommittee only has two options with respect to its enforcement of Title XI: de-certifying a state's entire appraiser certification program or jawboning its licensing agency to take actions required to put it into Title XI compliance. Neither option is adequate. Rulemaking authority is a time-tested, fair and cost-effective way not only to ensure state agency compliance with Title XI requirements but to ensure reasonable enforcement uniformity among the states (see Problem 3 below).

Recommended solution: Give the Subcommittee rulemaking authority.

(3) Problem: The regulation of appraisers by the states has been uneven. The regulation of real estate appraisers by the licensing boards of the 50 states, the territories and the District of Columbia has been disturbingly uneven and, in some cases, borders on ineffectual. Title XI contemplated a reasonable degree of uniformity and certainty in the way states would enforce compliance with the ethics, competency and other protocols of professional appraisal practice. Based on reports from our real estate valuation members, this is not happening to an adequate degree.

Recommended solution: Ask the GAO, which did a good job fleshing out the landscape of Title XI's regulatory environment, to examine this issue and make recommendations on what states and the federal government need to do to improve the consistency and effectiveness of state compliance efforts.

(4) Problem: Improvements in state reciprocity agreements and temporary practice permits are required.

(a) Some states make the issuance of temporary practice permits difficult and costly to obtain. Title XI recognized that real estate-related financial transactions requiring appraisal services are national (and often international) in scope, often requiring appraisers to travel from state to state on temporary practice assignments for a client. As a result, Title XI required states not to erect barriers to the issuance of temporary practice permits. Although local appraisers generally perform valuations of single-family properties in connection with mortgage financings, there are many

instances in which national and regional mortgage lenders, real estate developers, insurance companies and real estate investment trusts/partnerships hire major valuation firms or appraisers with a valuation specialty niche (e.g., hotels, strip shopping malls, office buildings) to appraise the market value of real estate in many states.

Notwithstanding the efforts of the Appraisal Subcommittee to break down the barriers of some states to temporary practice, the problem remains.

Recommended solution: A consensus is developing between appraisers and major users of their services in support of a “driver’s license” approach to temporary practice. Title XI should be amended to provide that appraisers duly certified or licensed and in good standing in one state must have their credentials honored in all other states for legitimate temporary practice purposes only.

(b) Reciprocity still needs improvement. In many areas of the country, real estate appraisers regularly practice on a multijurisdictional basis. The District of Columbia Metropolitan Area (D.C., Maryland and Virginia) is a typical example of a situation where an appraiser certified or licensed in one jurisdiction is likely to have clients in the other two jurisdictions. Because states frequently differ in their qualifications requirements for licensing or certification and because each state has its own fee structure, it is impractical and inefficient for an appraiser to obtain an original certification/license from each jurisdiction. Title XI contemplated easy reciprocity between and among states in situations where appraisers live and practice near borders with other jurisdictions.

Recommended solution: Title XI should be amended in a way that requires states to enter into mutually beneficial reciprocity agreements that facilitate interstate commerce.

(5) Problem: Because each state's appraiser licensing board currently must approve all primary and continuing education courses offered its licensees and licensee applicants, hardships are imposed on national education providers and practitioners. Professional appraisal societies offer their members and other qualified individuals a wide range of valuation course work. Providing continuing education to its members from across the country is a central feature of ASA's annual conferences. The hardship on education providers is created when ASA—and other national appraiser education providers—must seek approval from each of the home states of its members in order for their continuing education credits to be accepted.

Recommended solution: A central clearinghouse should be established for the purpose of approving appraiser education course work for all states.

(6) Problem: The Appraiser Qualifications Board of the Appraisal Foundation lacks authority to establish qualification requirements for licensed appraisers in federally related transactions. An amendment to Title XI, approved approximately two years after its enactment, severely limited the authority of the Appraisal Foundation to establish qualifications for licensed appraisers in federally related transactions. The result is an anomalous public policy situation in which the foundation is able to establish qualifications for certified appraisers but not for the lesser-skilled licensed appraisers.

Recommended solution: ASA respectfully urges the Banking Committee to amend Title XI by restoring the foundation's authority to set minimum qualification requirements for licensed appraisers. The limitation on that authority was driven by a

concern—among some mortgage market players—that the Qualifications Board would set qualification requirements so high that a shortage of appraisers would be created. Although that concern was highly dubious when it was made a decade ago, it has no validity today. Ironically, the concern today within the professional appraisal community and for many government officials is that qualifications for licensed appraisers in a number of states are inadequate. And, it is long past the time to end the illogical public policy disconnect between the Qualifications Board’s authority to set standards for certified appraisers but not for licensed appraisers.

(7) Problem: The federal bank regulatory agencies, by rulemaking, have limited the application of Title XI’s professional appraisal and uniform standards requirements to loans above \$250,000 for residential property and \$1 million for commercial property. When Title XI was enacted in 1989, it included a de minimis of \$15,000. Although federally insured financial institutions and the GSEs are free to apply Title XI’s provisions to transactions below the “de minimis” levels (and many do), ASA regards their establishment as unnecessarily jeopardizing “safety and soundness.” The Uniform Standards of Professional Appraisal Practice permit certified and licensed real estate appraisers to tailor their services to meet their customers’ needs as to speed and cost, without violating USPAP’s ethics provisions. Accurate valuations of the collateral for loans by federally insured financial institutions are an indispensable safety and soundness component of a federally related real estate transaction.

Recommended solution: ASA urges the Banking Committee to request a GAO study of the de minimis issue, including an analysis of its safety and soundness consequences.

Conclusion

The American Society of Appraisers believes that the real estate appraiser certification and licensing system established by Title XI is working successfully to protect not only federal financial interests but the interests of consumers and the appraisal profession as well. ASA looks forward to working with the Senate Banking Committee to build on the current system for the purpose of strengthening it and correcting current weaknesses. I would be glad to answer any questions you may have.

Attachment 1

American Society of Appraisers: Fact Sheet

The American Society of Appraisers (ASA) is the only appraisal society in the United States that represents appraisers of all types of property—real, personal and intangible. ASA has more than 6,000 professional members committed to providing consumers the best valuation expertise available. An international organization, ASA was founded in 1936 and is currently headquartered outside of Washington, D.C., in Herndon, Va.

For nearly 70 years, ASA has fostered professional excellence.

- ASA accredits members only after they complete a rigorous testing and evaluation process that requires years of study, training and peer review.
- ASA ensures that its accredited appraisers provide consumers and businesses with independent opinions of value.
- ASA provides continuing education programs and training opportunities to members;
- ASA maintains a strong role in the Appraisal Foundation, a nonprofit organization recognized by the U.S. Congress as the sole source for uniform appraisal standards and qualifications; and
- ASA requires all its members to subscribe to the Appraisal Foundation's Uniform Standards of Professional Appraisal Practice (USPAP) and ASA's Principles of Appraisal Practice and Code of Ethics, which the society enforces through a grievance process that allows clients to challenge appraisals rendered by ASA members.

ASA members come from all 50 states, Puerto Rico, the U.S. Virgin Islands and 44 foreign countries (including Canada, Mexico, China and the Philippines) and represent the following disciplines:

- **Appraisal Review and Management:** This discipline requires practitioners to manage multidiscipline appraisal practices, review appraisals performed by others and report the results of those reviews.
- **Business Valuation (BV):** Business valuation appraisers value intangible assets—patents, trademarks, copyrights, intellectual property; provide independent, unbiased opinions of values for businesses; and prepare merger and acquisition analysis and other studies. BV appraisers work for large accounting and financial consulting firms.
- **Gems and Jewelry:** ASA appraisers and Master Gemologist Appraisers assess every kind of gem and jewel, from mineral specimens and rough stones to art, designer, antique and period jewelry.
- **Machinery and Technical Specialties:** Professional appraisers value machinery and equipment, cost surveys, aircraft, boats, oil and gas, mines and quarries, public utilities, IT property and natural resources. They provide appraisals for Fortune 500 and other companies for the purposes of sale, acquisition, ad valorem tax, eminent domain, collateralization or insurance.
- **Personal Property:** In this discipline, appraisers value art, antiques, books, automobiles, and residential contents, including every possible type of property from African sculpture to wines.
- **Real Property:** These appraisers may specialize in property that is urban, residential, ad valorem, rural or timberland (including the land, improvements and all associated structures and additions). ASA appraisers can produce appraisals for acquisition or disposition, mortgages, insurance, estate taxes, etc.

Many ASA members are widely recognized experts and pioneers in their fields. They include

- the founders of the business valuation appraisal profession, which comprises valuers of business and business interests of all sizes, from sole proprietorships to Fortune 500 companies;
- the personal property appraisers called on to appraise highly visible and valuable items such as gifts given to the First Family by foreign dignitaries and a collection of Princess Diana's dresses;
- the foremost expert in the field of "celebrity valuation," which involves appraising the value of a celebrity's brand and image along with his or her physical possessions;
- virtually all appraisers accredited in the appraisal of machinery and equipment and technical properties; and
- dozens of experts hired to appraise the value of the businesses, real property, personal property, machinery and equipment, and jewelry destroyed in the September 11 attack on the World Trade Center.

For more information, call Ted Baker, ASA executive vice president, at (800) 272-8258, ext.

109, or go online to www.appraisers.org.